

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

| | | |
|--|---|----------------|
| THE APPLICATION OF SOUTH HOPKINS WATER |) | |
| DISTRICT FOR A RATE ADJUSTMENT UNDER THE |) | CASE NO. 10098 |
| PURCHASED WATER ADJUSTMENT CLAUSE |) | |

O R D E R

Procedural Background

On November 13, 1987, South Hopkins Water District ("South Hopkins") filed its revised tariff sheets with the Commission for the purpose of adjusting its rates pursuant to KRS 278.015 and Commission Regulation 807 KAR 5:068. Before the Commission had completed its review of these revised tariff sheets, South Hopkins on December 14, 1987, moved to suspend all action in this case.

On December 21, 1987, South Hopkins withdrew the revised tariff sheets and petitioned the Commission for a deviation from 807 KAR 5:068. It sought permission to retain its existing rates and all monies recently refunded to it by Dawson Springs Municipal Water and Sewer System ("Dawson Springs").

At the request of Commission Staff, an informal conference was held on January 27, 1988 between Staff and representatives of South Hopkins to discuss this petition.

On February 22, 1988, South Hopkins withdrew its petition and substituted another which requested that South Hopkins be declared a producer of water. In this new petition, South Hopkins also offered to reduce its rates to their levels as of September 1,

1986 and to refund all revenue collected in excess of those rates due to a rate adjustment granted in Case No. 9700, Purchase Water Adjustment of South Hopkins Water District, final Order dated October 17, 1986.

Discussion

South Hopkins obtains its water from Dawson Springs Municipal Water and Sewer System. Dawson Springs calculates its water production costs annually and bills South Hopkins retroactively for the additional cost of water sold to it during the prior year. After conducting an audit for the 12 months ending June 30, 1987, Dawson Springs decreased its rate for water from \$.97663 to \$.87879 per 1,000 gallons, effective July 1, 1986. As a result of this decrease in its unit cost of water, Dawson Springs refunded \$22,546 to South Hopkins on October 23, 1987.

Commission Regulation 807 KAR 5:068, Section 2(3), requires a water district to reduce its rates accordingly when a supplier reduces its base rate. Furthermore, any refund to a water district by a supplier for overpayments must be flowed through to its customers within 2 months of the refund. 807 KAR 5:068, Section 2(4).

To avoid the application of this regulation,¹ South Hopkins argues that it is a joint producer of water. It claims to be involved in a joint venture with Dawson Springs to operate and

¹ Commission Regulation 807 KAR 5:068 applies only to water districts which have specifically invoked this regulation to adjust their rates. Having invoked it, a water district is bound by its provisions. South Hopkins applied and was granted an upward adjustment in rates under this regulation in Case No. 9700.

maintain Dawson Springs' water filtration plant. An examination of the South Hopkins-Dawson Springs water purchase contract and circumstances surrounding its creation, South Hopkins asserts, will show that the parties intended, and created, a joint venture for the operation of a water filtration plant.

Since South Hopkins' inception in 1965, Dawson Springs has been its sole source of water. In their original agreement, South Hopkins contracted with Dawson Springs to provide all its water requirements at the "prevailing rate charged single commercial establishments within the corporate limits of Dawson Springs." As both utilities' demand for water increased, Dawson Springs' existing water treatment facilities were unable to keep pace.

The need for a larger water filtration plant spurred Dawson Springs and South Hopkins to enter a water purchase agreement in 1978. Funding from the Farmers Home Administration was expressly conditioned upon Dawson Springs obtaining a long term water purchase agreement with South Hopkins. The water district, in turn, was about to add 500 more families to its system and needed an assured source of water. The situation was best summarized by the Dawson Springs City Commission which declared in a resolution authorizing an agreement that "said proposal for a joint source of supply is to the mutual advantage of the City of Dawson Springs and the South Hopkins Water District."

The terms of the water purchase agreement evidence an intent among its parties to create a more involved relationship than that of purchaser and seller. The preamble of the agreement states that the parties intend "to share in the cost of constructing said

water treatment plant." Unlike the earlier contract between the parties where the cost which South Hopkins paid for water was entirely within the discretion of Dawson Springs, the 1978 agreement attempts to allocate costs equally between the parties based upon the actual cost of water produced and actual water usage. Neither party can benefit at the other's expense from the water plant's operation. Furthermore, the cost of water does not include costs associated with Dawson Springs' other facilities. The agreement, which runs until the year 2023, requires both parties to assist in enlarging the water filtration plant's capacity when demand reaches certain levels. South Hopkins is given some control over the plant's operation by its right to question specific items of the plant's operation and maintenance costs.² Both parties are required to contribute to a "water supply facility reserve fund" to cover extraordinary expenses associated with the a water filtration plant.

Sufficient evidence exists to support a finding that the 1978 agreement between Dawson Springs and South Hopkins created a joint venture to operate the water filtration plant. A joint venture exists where two or more parties combine their money, property, efforts, knowledge and skill to a common undertaking in which each party has the right of mutual control and shares its benefits and burdens. 46 Am.Jur.2d Joint Ventures §1 (1969). In this case, both parties have a mutual interest in and some degree of control

² South Hopkins has exercised this authority in past years. Response to Commission Order of March 21, 1988, Item 12.

over the water filtration plant's operation.³ Both have contributed their money and effort to the plant. Both share the burdens and benefits of the plant's operation.

We find that South Hopkins and Dawson Springs are involved in a joint venture to operate and maintain a water filtration plant and are, thus, joint producers of water. As 807 KAR 5:068 applies only to water districts which are not self-sufficient producers of water, it cannot apply to South Hopkins.

In whatever light the relationship between South Hopkins and Dawson Springs is viewed, it is clear that Commission Regulation 807 KAR 5:068 does not adequately address South Hopkins' situation. The regulation is designed to allow water districts to recover their cost for purchased water without resort to general rate case proceedings by merely passing any change in their supplier's rates on to their ratepayers. It has required South Hopkins, however, to absorb large increases in the cost of water without any hope of recovery from its ratepayers.

Under its existing agreement with Dawson Springs, South Hopkins pays only for the cost to produce the water. The cost of water production is determined by an annual audit. Based upon the results of this audit, a rate for water is determined. For the 12 months following the audit, South Hopkins makes monthly payments

³ South Hopkins acknowledges having less control over the plant's operation than Dawson Springs. Unequal control of operations, however, does not prevent the existence of a joint venture. See Flanders v. U.S., 172 F.Supp. 935 (1959); Fishback v. U.S., 215 F.Supp. 621 (1963).

to Dawson Springs at this rate. When the next annual audit is performed, the precise cost of water used by South Hopkins during the previous 12 months is determined. If the total cost of water exceeds South Hopkins' total payments, South Hopkins must pay the difference to Dawson Springs. If total payments exceed total cost, the overpayment is refunded to South Hopkins. The rate is then adjusted to reflect the results of the recent audit. South Hopkins' monthly payments for the following 12 months will be based at this new rate.

Commission Regulation 807 KAR 5:068 does not allow South Hopkins to recover from its customers any additional payments made to Dawson Springs to cover underpayments. It covers only prospective increases in suppliers' rates, not retroactive increases. South Hopkins must, therefore, absorb these retroactive increases. Because the regulation requires a water district to refund to its customers any refund received from a supplier, 807 KAR 5:068, Section 2(4), these absorbed increases cannot be offset by any refunds from Dawson Springs for overpayments.

Since 1984, the regulation has failed to prevent South Hopkins from having to absorb approximately \$21,000 in increases in the cost of water. In October 1984, the Commission granted a general rate increase to the water district.⁴ After an audit was conducted in July 1985, South Hopkins was required to pay \$11,453

⁴ Case No. 9106, South Hopkins Water District's Notice of Adjustment of Rates and Application Pursuant to 807 KAR 5:001, Section 9, For Authority to Adjust Rates, Final Order dated October 3, 1984.

to Dawson Springs for underpayments. After the audit of July 1986, the district was required to make an additional \$9,502 payment to Dawson Springs. Neither payment could be recovered under the regulation. In October 1986, South Hopkins sought and was granted an increase in rates pursuant to the regulation. After the July 1987 audit, Dawson Springs refunded \$22,546 to South Hopkins and lowered its rates to reflect lower costs of water production. Under the terms of the regulations, South Hopkins may not retain this refund but must pass it through to its ratepayers. South Hopkins must also lower its rates, making it vulnerable to another underpayment should water costs rise to their past historic levels.

If South Hopkins is to be freed from the dictates of 807 KAR 5:068, we believe that it should also disgorge any benefits received from this regulation. South Hopkins has offered to refund \$12,373 over a 2-month period at a rate of \$.48 per 1,000 gallons of water. Its offer is based on the per unit increase of \$.06 per 1,000 gallons granted in Case No. 9700 and on its water sales during the 16-month period in which this increase was in effect.⁵ South Hopkins also proposes to reduce its rates to the levels approved in Case No. 9016. As these actions will eliminate

⁵ Gallons sold 206,214 m. gals. x .06 = \$12,373.
Projected sales 206,214 m. gals. + 16 mo. = 12,888 gals.
12,888 gals. x 2 mo. = 25,776 m. gals.
Per unit refund amt. \$12,373 + 25,776 m. gals. = \$.48 per
1,000 gallons.

all benefits which South Hopkins received from 807 KAR 5:068,⁶ we accept South Hopkins' offer.

FINDINGS AND ORDERS

The Commission, having reviewed the evidence of record and being advised, finds that:

1. South Hopkins and Dawson Springs are involved in a joint venture to operate and maintain a water filtration plant and are, thus, joint producers of water. This water filtration plant provides all of South Hopkins' water.

2. As South Hopkins is a producer of water, Commission Regulation 807 KAR 5:068 does not apply to it.

3. South Hopkins' offer to refund additional revenue collected as a result of the rate adjustment granted in Case No. 9700 and to reduce its rates to those approved in Case No. 9016 should be accepted.

IT IS THEREFORE ORDERED that:

1. South Hopkins be, and it hereby is, declared a joint producer of water.

2. South Hopkins' offer to refund additional revenue collected as a result of the rate adjustment granted in Case No. 9700 and to reduce its rates to those levels approved in Case No. 9016, be, and it hereby is, accepted.

3. Effective immediately South Hopkins shall charge the rates contained in the Appendix to this Order.

⁶ Since its creation in 1965, South Hopkins has sought and been granted only one rate adjustment pursuant to 807 KAR 5:068.

4. South Hopkins shall refund the amount of \$12,373 to its customers at a rate of \$.48 per 1,000 gallons of water over the next 2 months or until such time as the refund has been completed.

5. South Hopkins shall file with the Commission, within 30 days of the date the refund is completed, a schedule showing the amounts of the refund and who received them.

6. South Hopkins shall file a tariff schedule reflecting its new rates within 30 days of the date of this Order.

Done at Frankfort, Kentucky, this 24th day of May, 1988.

PUBLIC SERVICE COMMISSION

Richard D. Weman, Jr.
Chairman

Robert M. Kline
Vice Chairman

James M. Williams
Commissioner

ATTEST:

Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 10098 DATED May 24, 1988.

The following rates and charges are prescribed for the customers in the area served by South Hopkins Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

| <u>Gallonge Blocks for Each Meter Size</u> | <u>Rate for Each Gallonge Block</u> |
|--|---|
| <u>5/8 Inch x 3/4 Inch Meter</u> | |
| First 1,000 gallons per month | \$6.25 (Minimum Bill) |
| Next 9,000 gallons per month | 2.75 per 1,000 gallons |
| Next 10,000 gallons per month | 2.35 per 1,000 gallons |
| Next 30,000 gallons per month | 2.00 per 1,000 gallons |
| Over 50,000 gallons per month | 1.50 per 1,000 gallons |
| <u>3/4 Inch Meter</u> | |
| First 5,000 gallons per month | \$17.25 (Minimum Bill) |
| Next 5,000 gallons per month | 2.75 per 1,000 gallons |
| Next 10,000 gallons per month | 2.35 per 1,000 gallons |
| Next 30,000 gallons per month | 2.00 per 1,000 gallons |
| Over 50,000 gallons per month | 1.50 per 1,000 gallons |
| <u>1 Inch Meter</u> | |
| First 10,000 gallons per month | \$31.00 (Minimum Bill) |
| Next 10,000 gallons per month | 2.35 per 1,000 gallons |
| Next 30,000 gallons per month | 2.00 per 1,000 gallons |
| Over 50,000 gallons per month | 1.50 per 1,000 gallons |
| <u>2 Inch Meter</u> | |
| First 20,000 gallons per month | \$54.50 (Minimum Bill) |
| Next 30,000 gallons per month | 2.00 per 1,000 gallons |
| Over 50,000 gallons per month | 1.50 per 1,000 gallons |
| <u>3 Inch Meter</u> | |
| First 50,000 gallons per month | \$114.50 (Minimum Bill) |
| Over 50,000 gallons per month | 1.50 per 1,000 gallons |